

Management's Discussion & Analysis

West Virginia Mutual Insurance Company

NAIC # 11972

December 31, 2012 and 2011

The West Virginia Mutual Insurance Company (the Mutual) completed its eighth full year of operations in 2012 and is the largest medical professional liability insurer in West Virginia. Comments on specific operating items follow:

1. Premiums

Written premium decreased 12.5% to \$28,690,738 from \$32,770,475 in 2011. This decrease was principally due to renewal credits and business lost to competition. While greater than the 7.8% decrease experienced in 2011, the current year decrease was reasonable based on the amount of the current year's renewal credit.

2. Assets

Admitted assets increased .1%, compared to a .5% increase in admitted assets in 2011. In 2011, the Company closed a large number of claims resulting in 63% greater payouts than in 2010. Cash flow was relatively flat in 2012, resulting in assets being unchanged from 2011. The amounts recoverable from reinsurers decreased to \$1,265,985 compared to \$2,652,768 in 2011. In 2011 there were a greater number of large claims closed near the end of the year on which the recoverable amount had not yet been collected resulting in a higher receivable. Admitted deferred tax assets also experienced a decrease of 21% to \$2,284,812 from \$2,893,353 in 2011 due to the take down in the reserves. These asset decreases are offset by an increase in the bonds held by the Mutual of \$3,000,000.

The Company's investments remain of strong quality and do not contain exposure to sub-prime mortgages, hedging strategies or other areas generally experiencing problems in recent markets. The Mutual has monitored its tax exempt bond portfolio to avoid states and municipalities having financial difficulties and has maintained an overall AA rating on its portfolio. All of the Mutual's bonds, except one NAIC 2 item totaling .6% of the portfolio, are listed as NAIC 1. Additionally, the Mutual has kept its portfolio in short duration (3.3 years) in an effort to guard against the effects of inflation which is

expected in the near future. During 2011, the Company made its first investment in common stocks using high quality dividend paying equities. This portfolio totals \$6,917,945 at December 31, 2012 including a 7.6% increase from original cost.

3. Liabilities

The Mutual's reported reserve position has decreased by 14.8% compared to 2011 reflecting decreases in report years 2007-2011. The 2011 reserves decreased 21.7% from 2010 reflecting decreases in all prior report years. These results reflect a consistent pattern in the Company's development and its conservative reserving policy as well as the drop in claim frequency, which has been country wide in the medical professional liability line. Overall, liabilities are down 12.4% from 2011 due primarily to the reduction in reserves. This compares to a 10.7% decrease in 2011.

4. Policyholders' surplus

Policyholders' surplus increased 12.6% and 14.9% in 2012 and 2011, respectively, driven by operating results for those years.

5. Operations

Losses from prior years were reduced by \$16.0 million in 2012 compared to \$17.3 million in 2011. These provisions are driven by lower than expected development of previously known cases and reflected in the Mutual's actuarial analysis.

The Company's principal reinsurance is a swing-rated program covering \$500,000 excess of \$500,000 for the Mutual's primary \$1,000,000 policy. The Company recorded \$1 million of expected reinsurance premium recoveries in 2012 as opposed to additional reinsurance premiums of \$2.9 million in 2011. The 2011 amount resulted from a large claim received in 2011. This claim was resolved favorably in 2012 allowing for the takedown of a portion of the expected additional reinsurance premiums. In 2012, the Mutual chose to commute the 2004-2007 reinsurance contracts. There was no negative impact to the Mutual's underwriting results from the recording of the commutation.

Expense ratios for 2012 and 2011 were 32.7 and 33.6%, respectively. As the ratio would indicate there was minimal change in underwriting expenses from last year.

The Mutual's effective tax rate was 24.6% and 26.3% in 2012 and 2011, respectively, reflecting profitable underwriting results for each of the past two years. The effective rate is lower than the statutory rate of 34% due principally to tax free investment income.

In summary, the Mutual's financial condition after eight and one-half years of operations is excellent. Leverage is low with net premiums to surplus at .25 to 1 and liabilities at .78 to 1. Adjusted capital is 19.6 times authorized control level risk based capital.

Submitted by: _____
Gary J. Schultz, CFO